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No. 03-1521

IN THE

Supreme Court of the United States

VISA U.S.A. INC.,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Second Circuit

REPLY BRIEF FOR PETITIONER

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REPLY BRIEF FOR PETITIONER

The Government does not dispute the fundamental importance of this case to the future of the nation's consumer credit markets. Nor does the Government deny the critical need for clarity in the rules governing the boundaries of acceptable competition between direct rivals. The Government suggests, however, that the case is not a worthy candidate for review because the rulings below were merely fact-bound applications of settled legal rules governing joint ventures.

Nothing could be further from the truth. The decisions below reflect numerous fundamental legal errors – errors which portend serious consequences for consumer credit markets and for cooperative business enterprises throughout the economy. In conflict with the decisions of this Court and others, the courts below erroneously applied a legal presumption disfavoring joint venture rules that restrain competition between competitors; they erroneously required Visa to prove that its loyalty rule was necessary to the survival of the venture; and they erroneously equated reduction in a *single competitor's* output with reduction in *overall competitive* output. The Government's brief in opposition does not explain or justify these errors. It simply repeats them. The Government's brief thus fails to make a persuasive case for denying review of this extremely important case.

1. The Government contends that the Second Circuit applied the proper legal standard to By-law 2.10(e) and did not invoke a rule disfavoring horizontal restraints in the joint venture context. As the Government tacitly acknowledges, such an approach *would* be at odds with decades of precedents from this Court and others. The Government argues, however, that the Second Circuit was merely rejecting Visa's contention that the restraint should be analyzed as similar to an exclusive distributorship arrangement. Opp. Br. 20.

The Government's reading of the decision is incorrect. The relevant discussion of horizontal restraints does come in

response to Visa's contention that, because By-law 2.10(e) does not in any way prevent Amex from reaching potential credit card purchasers, it causes no more harm to competition than does an exclusive distributorship arrangement that does not prevent competitors from getting to market.[1] But to refute that analogy, the Second Circuit unambiguously enunciated a rule applicable to all horizontal joint venture restraints. After laboring to establish the obvious point that By-law 2.10(e) constitutes an agreement among competitors, the court treated that fact as if it were a virtual death knell:

> Visa U.S.A. and Mastercard . . . are not single entities; they are consortiums of competitors. . . . The competitors have agreed to abide by a restrictive exclusivity provision to the effect that in order to share the benefits of their association by having the right to issue Visa or MasterCards, they must agree not to compete by issuing cards of AmEx or Discover. The restrictive provision is a horizontal restraint adopted by 20,000 competitors. . . . Each has agreed not to compete with the others in a manner which the consortium considers to be harmful to its combined interests. Far from being "presumptively legal," such arrangements are exemplars of the type of anticompetitive behavior prohibited by the Sherman Act.

Pet. App. 20a. In the end, that language will speak for itself – and, unfortunately, it will speak volumes to courts and practitioners evaluating the propriety of horizontal restraints in the joint venture context.

It is of no moment that immediately after describing joint venture horizontal restraints as "exemplars" of illegality, the court cited a string of "rule of reason" cases. Opp. Br. 20-

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[1] *See Jefferson Parish Hosp. Dist. No. 2 v. Hyde*, 466 U.S. 2, 45 (1984) (O'Connor, J., concurring) ("Exclusive dealing is an unreasonable restraint on trade only when a significant fraction of buyers or sellers are frozen out of a market by the exclusive deal.").

21. If anything, the citation only illuminates the court's fundamental legal error. The first case cited is this Court's opinion in *NCAA v. Board of Regents*, 468 U.S. 85 (1985), from which the Second Circuit quotes the observation that "member institutions have created a horizontal restraint – an agreement among competitors on the way in which they will compete with each other," *id.* at 99; *see* Pet. App. 20a. The Second Circuit mistakenly reads this language as presumptively condemning joint venture horizontal restraints as "exemplars" of illegality. In fact, as explained in the petition, Pet. 17, the Court in *NCAA* generally *applauded* the NCAA's "agreement among competitors" because it "enable[d] a product to be marketed which might otherwise be unavailable," thereby "widening consumer choice," 468 U.S. at 102. The Court only invalidated one specific rule of the venture because that rule clearly increased the prices and restricted the output of televised football games. *Id.* at 114. That is exactly how joint venture restraints should be analyzed. Nothing in *NCAA* remotely suggests that the Court regarded the NCAA's rule as suspect simply because it was an agreement among competitors. Quite the contrary, the Court indicated that the rule might have been upheld if the NCAA had adopted it "in order to enhance its ability to compete" against "interbrand competition" (i.e., competition from another collegiate football league). Because the NCAA faced no such competition, the rule could not be justified. Visa, of course, does face vigorous "interbrand" competition, and By-law 2.10(e) indisputably enhances its members' ability to compete against Visa's rivals in the payment card market.

For that reason, By-law 2.10(e) should have been analyzed not as a presumptively unlawful horizontal restraint on competition, but as a presumptively *lawful* restraint ancillary to a pro-competitive joint venture. The Government acknowledges that "[l]oyalty rules that bar co-venturers from competing with their joint enterprise will often be found to be pro-competitive ancillary restraints," Opp. Br. 17, and

that, to be treated as ancillary, a restraint need only be "substantially" or "reasonably" related to the pro-competitive goals of the joint venture. *Id.* at 18, 10. The Government argues that the lower courts in this case correctly refused to treat By-law 2.10(e) as an ancillary restraint, *see id.* at 17, because they held that By-law 2.10(e) was not "reasonably related to the efficiency of the joint venture[]," *id.* at 19-20.

The courts below held no such thing. Although the courts *should* have applied a standard of "reasonable" or "substantial relationship" to the joint venture's pro-competitive goals, they actually applied a standard of *absolute necessity*. *See, e.g.*, Pet. App. 22a, 157a, 166a-67a. As the district court put it, Visa had not proved a need for the rule to protect its "fragile association." *Id.* at 157a. That standard of "necessity" is not the standard of "reasonable relationship" the Government now concedes should have been applied.[2]

Under the correct legal standard, it is clear that By-law 2.10(e), which simply prohibits members from competing directly with the enterprise, is the *archetypal* ancillary restraint. *See* Pet. 7-8, 15. The rule indisputably enables Visa's members to compete better against the venture's rivals in issuing payment cards, and thus is reasonably related to the venture's pro-competitive goal of enabling its members to compete in the payment card market. Nothing more should have been needed to establish a presumption of lawfulness in favor of By-law 2.10(e).[3]

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[2] *See NFL v. NASL*, 459 U.S. 1074, 1079 (1982) (Rehnquist, J., dissenting from denial of certiorari) ("The antitrust laws impose a standard of reasonableness, not standard of necessity."); Pet. 22 n.9.

[3] The Government contends that the lower courts properly relied on "duality" (*see* Pet. 7-8 & nn.3&4) to "find" that the loyalty justification for By-law 2.10(e) is pretextual: if the rule were genuinely necessary for Visa's survival, the Government insists, Visa would not allow its members to join Mastercard, its main rival. Opp. Br. 19 (citing Pet. App. 51a). But the courts' "finding" merely reflects their legal error in assum-

The Government correctly points out that courts have "invalidated anticompetitive agreements (including bylaws) even when imposed by legitimate, procompetitive joint ventures." Opp. Br. 17-18. But nobody contends that all joint venture rules are valid per se. Our point is that a by-law reasonably related to the goals of a pro-competitive joint venture should be invalidated only if a clear and unambiguous standard is met: the rule reduces output or increases prices. Because the courts below plainly did not apply that standard, they invalidated By-law 2.10(e) absent a proper showing of competitive harm, as we explain below.

2. The Government defends the decisions below as consistent with rule of reason standards on the ground that the district court "identified in detail five distinct types of harm" to competition." Opp. Br. 13. But *nothing* in the district court's discussion of "harm" reflects the type of harm legally sufficient to invalidate a presumptively lawful horizontal restraint, *see* Pet. 20-21, further confirming that the court applied the wrong legal standard to the record evidence. The Government's brief does not demonstrate otherwise.

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ing that Visa can adopt only those rules that are necessary for its operation, as opposed to those reasonably related to its pro-competitive goal of enabling its members to compete effectively in the payment card market. In any event, the Government does not deny that "triality" or "quadrality" would undermine Visa's competitive strength much more than "duality" has. *See* Pet. 8 n.4. Because conflicting incentives arise primarily when elite members of a venture are invited to join with a rival *that other venture members cannot join* – giving the elite members the incentive to undermine the venture while still remaining members – it is rational for Visa's members to have acquiesced in "duality" with an "open system" rival while not allowing themselves to join with "closed system" rivals.

The evidence concerning Visa's ability to function in certain international markets where By-law 2.10(e) does not apply (Opp. Br. 19) would also be virtually irrelevant under a threshold standard requiring something less than "necessity." In any event, the Government's own expert conceded at trial that foreign markets cannot be meaningfully compared to U.S. markets for this purpose. Tr. T-3529-3530.

First, the Government cites the district court's conclusion that By-law 2.10(e) "forestall[s] competitively significant product innovation." Opp. Br. 14. But the pages cited by the Government (Pet. 152a-54a) address the Amex "Blue" card, which, the court explicitly observed, has *already* "been a success for American Express." Pet. 153a. The court cited nothing about By-law 2.10(e) that affirmatively precludes or even hinders Amex from responding to consumer demand for more Blue cards, to the extent such demand exists. Rather, the court's discussion merely explains why invalidation of By-law 2.10(e) would enable Amex to tap into the distribution skills of Visa's members and thereby increase the general availability of the Blue card at minimal cost to Amex, *see id.* at 152a-54a – an outcome the court blithely *assumes* that consumers would prefer, if it were judicially mandated for them. The court's belief that consumers would be better off if Visa's main rival were more successful is plainly no basis for antitrust liability. *Cf.* Easterbrook, *The Limits of Antitrust*, 63 Tex L. Rev. 1, 3 (1984) ("In most cases even a perfectly informed court will have trouble deciding what the optimal long-run structure of the industry is, because there is no 'right' balance between cooperation and competition. The judge has no benchmark. Small wonder that the history of antitrust is filled with decisions that now seem blunders.").[4]

Second, the Government points to the courts' tautological conclusion that because By-law 2.10(e) prohibits Visa's members from dealing with Amex, the rule prevents Amex

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[4] The Government claims, without evident irony, that "the market, rather than competitors acting in concert, should decide whether and what innovations in product quality are important." Opp. Br. 14. But here it is *not* the market, but the *courts*, that will have decided whether and what innovations in product quality are so important that private decisionmaking – which created the joint ventures that spawned the nation's robustly competitive payment card markets – should now be subjected to judicial correction.

from dealing with Visa's members. Opp. Br. 15. The Government observes that restraints in "upstream or input markets" *can* harm consumers in theory, and thus "there is no basis for special tolerance of conduct restraining competition in upstream or input markets." *Id.* This is true but misses the point: when the "upstream" restraint is a presumptively lawful joint venture rule, "downstream" harm to consumers cannot be presumed, but must be proved. *See, e.g., Northwest Wholesale Stationers, Inc. v. Pac. Stationery & Printing Co.*, 472 U.S. 284, 294 (1985). The Government's defense of the courts' presumption that Visa's "upstream" horizontal restraint causes "downstream" harm confirms, yet again, that the courts applied the wrong legal standard to the restraint.

Third, finally addressing the relevant test for competitive harm, the Government asserts that the district court found that By-law 2.10(e) has "the effect of 'reducing overall output.'" Opp. Br. 16 (quoting Pet. App. 119a-20a). The court found nothing of the kind. Even the Government is able to point only to the court's observation that Visa member Advanta considered issuing three million Amex cards as evidence of output reduction, *id.* (citing Pet. App. 129a-31a), but this of course shows only that By-law 2.10(e) reduced *Advanta's* output of *Amex* cards by three million – it does nothing whatsoever to show that By-law 2.10(e) reduced the *overall output of the payment card market* by three million cards. In fact, it is simply undisputed that the rule has *not* reduced overall output: if there is consumer demand in the market for three million more Amex cards, or three million more Advanta Visa cards, or three million more cards of any kind issued by any issuer, it is absolutely clear that the demand could and would be easily met.

Indeed, the district court's discussion of what it regards as "output reduction" only highlights the court's improper focus on harm to Amex as conclusive proof of harm to competition. As the district court itself described its fundamental finding of the "ouput reduction" effected by By-law 2.10(e):

"As a result [of the rule], American Express and Discover are forced to operate as single-issuer networks, limiting their transaction and issuance volume and stunting their competitive vitality." Pet. App. 120a. It is of course absurd to suggest that Amex – the single largest card issuer in the United States – possesses anything other than the most intense competitive vitality despite By-law 2.10(e). Yet the more basic legal flaw in this "finding" is its patent conflation of harm to a competitor's sales volume with harm to overall competitive sales volume. There has been no showing whatsoever of the latter. To the exact contrary, during the entire period By-law 2.10(e) has been in force, the payment card market has been characterized by dramatically *expanded* output, rapidly falling (even negative) prices, significant innovation, and increases in quality and consumer satisfaction. None of those facts is in dispute.

Fourth and *fifth*, the Government contends that elimination of By-law 2.10(e) would increase competition for merchant acceptance of payment cards, leading to increased merchant acceptance of Amex and Discover cards, which in turn would benefit consumers by giving them even greater choices in payment card uses than they already have. Opp. Br. 16. This is yet another – especially unabashed – equation of harm to rivals with harm to competition. As the Government recognizes, the proper test for competitive harm is not the rate of merchant acceptance per se, but the effect of that acceptance on consumers. *Id.* The Government's explicitly stated assumption, however, is that consumers want to be able to use Amex cards even more than they already can – so much more so that judicial intervention in the robustly competitive payment card market is necessary to ensure that merchant acceptance rates change, such that consumers can get what the court believes they "really" want, i.e., more Amex card usage. That is a manifestly indefensible view of the role of antitrust law in a competitive market economy.

3. The Government denies that the decision below conflicts with any other circuit decision, but the distinctions it draws are either wrong or irrelevant. For example, addressing *SCFC ILC, Inc. v. Visa U.S.A. Inc.*, 36 F.3d 958 (10th Cir. 1994) ("*MountainWest*"), the Government emphasizes a purely formal distinction: the rule at issue there (By-law 2.06) prevented an intersystem competitor from becoming a Visa member, whereas the rule at issue here prevents a Visa member from issuing the cards of an intersystem competitor. Although the Government gamely insists that the distinction is material, it does not deny that "both rules enforce the exact same loyalty principle: an entity cannot be a member of the Visa venture while issuing payment cards in competition with the venture." Pet. 23.

The Government attempts to distinguish *MountainWest* on the ground that By-law 2.06 merely precluded the addition of "one more Visa issuer" to an atomistic issuing market and thus did not significantly harm consumers. Opp. Br. 25. By contrast, the Government says, By-law 2.10(e) precludes banks from dealing with Amex and thus "prevent[s] consumers from obtaining products available only by combining" the special skills of Amex and Discover with the special skills of Visa's member banks. *Id.* This is no distinction at all: the *MountainWest* court explicitly rejected *exactly* the same claim about consumer harm, *viz.*, that By-law 2.06 impermissibly reduced consumer choice because it hindered Discover's ability to issue a card that combined features of both the Discover and Visa networks. *See* Pet. 25. As the Tenth Circuit held, in irreconcilable conflict with the analysis and result in this case, there was no consumer harm *as a matter of law* – the court reversed a jury finding of liability – because the record showed, as it does here, that Visa's rival could already reach consumers with new products entirely on its own, even though that rival might "compete more effectively" absent the loyalty rule. 36 F.3d at 972.

The Government's effort to distinguish By-law 2.10(e) from By-law 2.06 by describing the former as a "much more like a group boycott" (Opp. Br. 25) is mystifying. The Government cannot mean by invocation of this pejorative label that a per se assumption of consumer harm is appropriate for By-law 2.10(e), though it was not for By-law 2.06. All agree that rule of reason analysis applies here, and this Court has previously held that horizontal restraints in the form of "exclusionary" joint venture membership rules do *not* presumptively harm consumers, even when they can be described theoretically as "group boycotts." *See Northwest Wholesale Stationers*, 472 U.S. at 294; *cf. NYNEX Corp. v. Discon*, 525 U.S. 128, 135 (1998) (when "no boycott-related *per se* rule applies," the plaintiff "must allege and prove harm, not just to a single competitor, but . . . to competition itself"). The "group boycott" label thus does nothing to distinguish By-law 2.10(e) from By-law 2.06. Each must be analyzed in terms of whether it harms competition by enabling Visa members to "increase price, decrease output, or otherwise capitalize on barriers to entry that potential rivals cannot overcome." 36 F.3d at 968. The courts in this case failed to apply that simple and clear standard to By-law 2.10(e).[5]

CONCLUSION

The petition for a writ of certiorari should be granted.

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[5] The decision below conflicts with *Rothery Storage & Van Co. v. Atlas Van Lines, Inc.*, 792 F.2d 210 (D.C. Cir. 1984), for the same reason. *Rothery* holds that a ancillary loyalty rule must be upheld as a matter of law so long as it does not decrease output and increase prices. *Id.* at 211. The courts here did not apply that standard to By-law 2.10(e). The Government submits that the decision below "does no violence to the accepted principles of joint venture law set forth in *Rothery*" because the lower courts found that the facts of this case present a greater threat to competition, Opp. Br. 27, but in fact the lower courts "found" a greater threat of competitive harm only because they did *not* apply the accepted principles of joint venture law set forth in *Rothery*.

Respectfully submitted,

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